

Fiscal Note



Fiscal Services Division

HF 226 – Geothermal Energy System Tax Credit (LSB1664YH)

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Fiscal Note Version – New

Description

<u>House File 226</u> revises the current residential Geothermal Heat Pump Tax Credit by increasing the tax credit percentage, expanding credit availability to corporate taxpayers, and changing the name to the Geothermal Energy System Tax Credit. The Bill takes effect on enactment and applies retroactively to tax year 2015 and after.

Background

Under current lowa law, the Geothermal Heat Pump Tax Credit is equal to 20.0% of the federal credit available for residential installations. That federal credit is equal to 30.0% of qualified installation costs. Therefore, the current lowa credit is equal to 6.0% of qualified installation costs. The current lowa credit is not refundable but unused portions may be carried forward for up to 10 tax years. The federal credit is set to expire December 31, 2016.

Under current federal law, there is a corporate investment tax credit available equal to 10.0% of qualified geothermal installation expenses at business locations. lowa does not currently have a corporate tax credit based on the federal business investment tax credit for geothemal installations. The federal credit for geothermal heat installations expires December 31, 2016. A companion federal credit for geothemal installations that produce electricity does not expire. The corporate tax credit proposed in this Bill will apply to both a geothermal heat installation and a geothermal electric generation installation.

Assumptions

- Given the current expiration date for the federal tax credit of December 31, 2016, the current
 and proposed credit for residential installations will cease to be available for residential
 geothermal installations after that date.
- Under current law and based on tax year 2013 tax credit claims, tax credit claims for tax year 2015 and tax year 2016 are projected to be \$2.0 million and \$2.1 million, respectively.
- For residential situations, the combined federal and state tax credit under current law is equal to 36.0% of installation costs. As proposed in this Bill, the combined tax credit will equal 48.0%. This increase in the tax subsidy is expected to increase residential installations in calendar year 2015 by 5.0% compared to current law, and by 20.0% for calendar year 2016. Projected claims for tax year 2015 and tax year 2016 are projected to equal \$6.3 million and \$7.6 million, respectively.
- This Bill includes a new lowa credit for business geothermal installations. The new credit is tied to a federal credit for geothermal heat and electricity installations. Based on the federal tax credit claims of lowa companies under those geothermal investment tax credit programs, claims for the proposed lowa 60.0% credit are projected to total \$228,000 for tax year 2015 and \$270,000 for tax year 2016. Those credit claims are all expected to be for heat installations. In addition, an assumption is made that no claims will be made for lowa installations of geothermal systems that generate electricity.
- The lowa geothermal tax credits for individuals and for corporations are not refundable or transferable but may be carried forward to future tax years. Tax credits that are not refundable or transferable take several tax years to redeem. It is assumed that for tax

- credits earned in a calendar year, the first redemptions take place in the next fiscal year and that it will take an additional five years for all credits from one year to be fully redeemed. **Table 1** below provides the assumed tax credit redemption pattern.
- Nonrefundable individual income tax credits reduce the tax yield of the local option income surtax for schools. Statewide, the average surcharge tax rate is equal to 3.2% of General Fund individual income tax revenue, net of refunds.

Table 1 Assumed Geothermal Energy Tax Credit Redemption Pattern									
	Individual Income Tax Credits - Current Law	Individual Income Tax Credits - Proposed Law	Corporate Tax Credits - Proposed Law						
Tax Year Earned	56.0%	48.0%	52.0%						
Tax Year Earned +1	30.0%	25.0%	17.0%						
Tax Year Earned +2	9.0%	9.0%	13.0%						
Tax Year Earned +3	5.0%	6.0%	8.0%						
Tax Year Earned +4	0.0%	6.0%	5.0%						
Tax Year Earned +5	0.0%	6.0%	5.0%						
Total % Redeemed	100.0%	100.0%	100.0%						

Fiscal Impact

The geothermal installation tax credit modifications and expansions contained in this Bill are projected to decrease net General Fund revenue by \$10.3 million over seven fiscal years, beginning in FY 2016. The projected impact by fiscal year is presented in the right-hand column of **Table 2**.

Table 2 Net General Fund Fiscal Impact Projection										
	Projected Tax Credit Impact Under Current		Individual Income Tax -		Corporate Income Tax -		General Fund Revenue			
FY 2016	\$	1,120,000	Pro \$	3,024,000	Proj \$	118,560	F	2,022,560		
FY 2017	Ą	1,776,000	Ą	5,203,800	Ų	179,160	۲	3,606,960		
FY 2018		810,000		2,457,000		75,540		1,722,540		
FY 2019		289,000		1,058,400		53,340		822,740		
FY 2020		105,000		831,600		33,000		759,600		
FY 2021		-		831,600		24,900		856,500		
FY 2022				453,600		13,500		467,100		
Total	\$	4,100,000	\$	13,860,000	\$	498,000	\$	10,258,000		

In addition, the individual income tax reduction will result in reduced tax revenue generated by the local option income surtax for schools. Surtax revenue is projected to decrease by the following amounts:

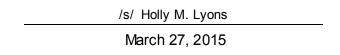
- FY 2016 = \$96,000
- FY 2017 = \$167,000
- FY 2018 = \$79,000
- FY 2019 through FY 2022 = \$25,000 each year

The federal tax credits for geothermal heat installations are set to expire December 31, 2016. Should the U.S. Congress extend the federal credits, the lowa credit will extend automatically. This will result in additional fiscal impact in future fiscal years.

Also, the federal credit for business geothermal electricity installations does not expire. If such a facility is constructed in lowa, the tax credit in this Bill will provide a corporate tax credit equal to 6.0% of the installation cost.

Sources

Department of Revenue Legislative Services Agency analysis



The fiscal note for this bill was prepared pursuant to <u>Joint Rule 17</u> and the lowa Code. Data used in developing this fiscal note is available from the Fiscal Services Division of the Legislative Services Agency upon request.